

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

NOTICE OF ADJUSTMENT OF THE RATES)	
OF KENTUCKY-AMERICAN WATER COMPANY)	CASE NO. 10481
EFFECTIVE ON FEBRUARY 2, 1989)	

ORDER ON REHEARING

On January 3, 1989, Kentucky-American Water Company ("Kentucky-American") filed its notice with the Commission seeking to increase its rates and charges effective February 2, 1989. The proposed rates would produce an annual increase in revenue of \$3,083,529, which Kentucky-American revised to \$3,234,892. On August 22, 1989, the Commission entered an Order that granted Kentucky-American rates which would produce an increase in annual revenues of \$2,475,296.

On September 11, 1989, the Utility and Rate Intervention Division of the Attorney General's Office ("AG") and the Lexington-Fayette Urban County Government ("LFUCG") filed a petition for rehearing, requesting the Commission's reconsideration of the following issues:

1. 30-Inch Raw Water Main
2. Deferred Tank Painting
3. Depreciation on the Toyota Advance
4. Extension Deposits
5. Case Working Capital
6. Other Rate Base Adjustments
7. Payroll
8. Plant Acquisition Adjustment
9. Belleville Laboratory

On the same day Kentucky-American filed a petition for rehearing, requesting the Commission to delay the issuance of a

final Order in this proceeding until after October 3, 1989. This would enable Kentucky-American to credit its customers bills, rather than issue checks, to pay the refunds required by the Commission's Order issued August 22, 1989.

30-INCH RAW WATER MAIN

The AG/LFUCG stated that they interpreted the Commission's decision in Case No. 10423¹ to mean that in this rate case the Commission would adhere to traditional rate-making and would not include post test-period investment in rate base. Based upon this interpretation, the AG/LFUCG failed to sponsor testimony at the hearing or argument in its brief regarding the economic effects of including the post test-period investment in rate base.

At the onset of this proceeding, Kentucky-American expressed its intent to recover the investment in the 30-inch raw water main either in Case No. 10423 or in this proceeding. Therefore, adequate notice was given that the 30-inch raw water main would be at issue in this case. The Commission finds that the AG/LFUCG has not shown good cause to substantiate why it failed to submit either testimony or argument in its brief on the 30-inch raw water main.

The Commission, in allowing the raw water main in rate base, stated that its decision was based in part on the review of Kentucky-American's monthly reports subsequent to the end of the

¹ Case No. 10423, The Tariff Application of Kentucky-American Water Company Procedure for Computing Revenue Requirements, Order dated May 9, 1989.

historical test period. The AG/LFUCG stated that it was unable to confront and cross-examine any post test-period monthly reports. The monthly reports referred to are not a part of the record in this proceeding; however, they are a part of the Commission's files and available for public inspection.

Based on the inability of the AG/LFUCG to review the monthly reports referenced in the Commission's Order, rehearing on this issue should be granted. The Commission is further of the opinion that Kentucky-American should file as a part of this case all monthly reports filed with the Commission subsequent to the end of the historical test period but prior to the August 22, 1989 Order, within 10 days from the date of this Order.

DEFERRED TANK PAINTING

The AG/LFUCG stated that it was unclear as to how the rate base level of deferred tank painting of \$1,003,235 was derived. The AG/LFUCG referenced footnote 8 and stated that the figures cited do not net to the amount included in rate base. However, footnote 8 shows total deferred tank painting and deferred tank painting amortization of \$1,606,810 and \$603,575, respectively. When deferred tank painting is reduced by the amortization, the result is \$1,003,235.²

The AG/LFUCG stated that it is also unclear as to whether their proposed adjustment to reduce deferred tank painting by \$41,381 was accepted or rejected by the Commission. The AG/LFUCG's proposed adjustment was included by Kentucky-American

² \$1,606,810 - \$603,575 = \$1,003,235.

in its revised exhibits and accepted by the Commission. However, the Commission reduced deferred tank painting by \$41,309, Kentucky-American's revised amortization adjustment.

Based on the aforementioned clarification, the Commission is of the opinion that the AG/LFUCG's request for rehearing on this issue should be denied.

DEPRECIATION ON THE TOYOTA ADVANCE

The AG/LFUCG requested rehearing on the issue of the Toyota advance to determine whether it is more properly characterized as a Contribution In Aid of Construction ("CIAC") and, therefore, should be reclassified. This issue is now being raised for the first time on rehearing. The AG/LFUCG argued that the investment is unique in that the advance was not provided by the ultimate customer and referenced the relative low number of refunds that were made during the test period.

The Uniform System of Accounts ("USoA") for Class A and B Water Companies states that customer advances, "shall include advances by or in behalf of customers for construction which are to be refunded either wholly or in part."³ The USoA also notes that the CIAC account shall not include advances for construction which are ultimately to be refunded wholly or in part.⁴ The Commission is of the opinion that the liability to refund the advance does exist and the source of the advance or the number of refunds made during a year are irrelevant in determining if an

³ 1988 USoA for Class A and B Water Companies, page 92.

⁴ Ibid., page 96.

advance should be classified as CIAC. The Commission is of the opinion that the AG/LFUCG's request for rehearing on this issue should be denied.

EXTENSION DEPOSITS

The AG/LFUCG stated that the Commission's rejection of their adjustment to reduce rate base by the 13-month average of extension deposits would allow Kentucky-American to earn a return on this source of non-investor capital. Extension deposits is a clearing account for customer advances that are to be refunded back to the advancing source within a 3-month period. It takes approximately 3 months for Kentucky-American to verify the existence of the new customers and then pay the refund due.

As stated in the August 22, 1989 Order, the ratepayers are receiving the benefit associated with the increased number of customers, and refunds are made within a relatively short time period. Therefore, it would appear that the amount to be earned from the interest on this account would be minimal and more than offset by the revenues provided by the new customers. However, the Commission is of the opinion that the AG/LFUCG's argument may have merit and wishes to hear further argument from the parties.

The Commission is of the opinion that the AG/LFUCG's request for rehearing on this issue should be allowed.

CASH WORKING CAPITAL

The AG/LFUCG stated that Kentucky-American's rate base was overstated as a result of cash working capital. The AG/LFUCG pointed to the difference in rate base and capital structure of \$1,289,535.

In its direct testimony, Kentucky-American stated that the 30-inch raw water main was to be funded by short-term investments and short-term debt of \$1,503,724 and \$1,000,000, respectively. The difference between the cost of the raw water main of \$2,046,345 and the short-term debt is \$1,046,345. Kentucky-American has funded this amount with its short-term investment and thus has accounted for the apparent shortfall in rate base. Accordingly, the AG/LFUCG's request for rehearing on this issue should be denied.

OTHER RATE BASE ADJUSTMENTS

The AG/LFUCG questions the derivation of the \$30,929 reduction to rate base which represents depreciation of the raw water main. The AG/LFUCG correctly notes that in the Revised Exhibit 3, Schedule 2, the deduction for depreciation of the raw water main was \$63,449. However, in a response filed on May 26, 1989, Kentucky-American amended the original adjustment to \$30,929. The reduced amount was due to the actual cost of the raw water main and the net salvage value of the replaced main.

The AG/LFUCG also stated that the Utility Plant Acquisition Adjustment was understated by \$25,198. The Commission determined that Kentucky-American had failed to reduce Utility Plant Acquisition Adjustment by a full 12-months' amortization and, therefore, increased rate base by \$25,198 to reflect the annualized amortization.

Based on the aforementioned clarification, the Commission is of the opinion that the AG/LFUCG's request for rehearing on this issue should be denied.

PAYROLL

The AG/LFUCG argued that the duties of the risk manager were formerly performed by the Service Company and, therefore, Kentucky-American should obtain a reduction in the Service Company charges. Consequently, the AG/LFUCG requested reconsideration of the adjustment to reduce Service Company charges.

Prior to December 1987, the Employee Relations Manager's duties included the monitoring of the program for risk management. Based on an analysis performed by Kentucky-American in December 1987, it was determined that the Employee Relations Manager's work load had increased substantially. The position of Risk Manager was created to lessen the work of the Employee Relations Manager. Therefore, it is evident that the Risk Manager's duties were performed in-house and not by the Service Company.

The Commission is of the opinion that the AG/LFUCG's request for rehearing on this issue should be denied.

PLANT ACQUISITION ADJUSTMENT

The Commission agreed with the AG/LFUCG's proposal to move the amortization of the negative plant acquisition adjustment above the line. However, the AG/LFUCG claimed that the amortization should be a non-taxable addition to income.

The Commission is of the opinion that the negative amortization is not income and thus deducted it from depreciation expense. This is in conformity with the Commission's treatment of positive amortizations.

The Commission is of the opinion that the AG/LFUCG's request for rehearing on this issue should be denied.

BELLEVILLE LABORATORY

Based on the volume of the testing performed by the Belleville Laboratory and the equipment leased by Kentucky-American, the AG/LFUCG has requested that their original adjustment be accepted. The AG/LFUCG stated that they do not seek to sever the relationship between Kentucky-American and the Belleville Laboratory, only to eliminate redundant and unnecessary expense.

The adjustment proposed by the AG/LFUCG is an elimination of the Belleville Laboratory costs from test-period operations. If the Commission adopted the adjustment as presented, the impact would virtually sever the relationship between Belleville and Kentucky-American.

The AG/LFUCG argued that the cost of the testing and the equipment acquired by Kentucky-American is not cost-efficient. However, it has failed to provide any evidence to support this contention. Thus, the Commission is of the opinion that the AG/LFUCG's request for rehearing on this issue should be denied.

CUSTOMER REFUND

Kentucky-American's petition for rehearing sought a delay until October 3, 1989 in the issuance of a final Commission Order. Based on the Commission's decision herein to grant rehearing on a limited number of issues raised by the AG/LFUCG, Kentucky-American's rehearing request is moot. Thus, Kentucky-American's request for rehearing should be denied.

SUMMARY

IT IS THEREFORE ORDERED that:

1. The AG/LFUCG's petition for rehearing be and it hereby is granted on the issues of the 30-inch raw water main and the extension deposits, and is denied on all other issues.

2. Kentucky-American's petition for rehearing be and it hereby is denied as being moot.

3. Kentucky-American shall file its monthly reports in the record of this case, with copies to all parties, within 10 days of the date of this Order.

Done at Frankfort, Kentucky, this 2nd day of October, 1989.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Executive Director